Supreme Court, U.S.
FILED
APR 19 1989
JOSEPH F. SPANIOL, JR.
CLERK

No. 88-1482

IN THE

Supreme Court of the United States

OCTOBER TERM 1988

THE CORPORATION COMMISSION
OF THE STATE OF OKLAHOMA,

Petitioner,

v.

ANR PIPELINE COMPANY, ET AL.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

PETITIONER'S REPLY BRIEF

LINDIL C. FOWLER, JR., ESQ.
General Counsel
Oklahoma Corporation Commission
400 Jim Thorpe Building
2101 North Lincoln Boulevard
Oklahoma City, Oklahoma 73105
(405) 521-2255

Counsel for Petitioner

April 19, 1989

Cone-Lewis Printing Co. • 16 N. College • Tulsa, OK 74110 • Phone (918) 832-8886

QUESTION PRESENTED

(same as in certiorari petition)

Is the State of Oklahoma pre-empted under the Natural Gas Act of 1938 and the Natural Gas Policy Act of 1978 from exercising regulatory authority over interstate pipelines pursuant to OKLA. STAT. tit. 52 §240?

PARTIES

Petitioner:

The Corporation Commission of the State of Oklahoma

Respondents:

ANR Pipeline Company
Colorado Interstate Gas Company
Columbia Gas Transmission Corp.
KN Energy, Inc.
Mississippi River Transmission Corp.
Natural Gas Pipeline Company of America
Tennessee Gas Pipeline Co.
Williams Natural Gas Co.
El Paso Natural Gas Company
Western Gas Interstate Company
Southern Natural Gas Company

TABLE OF CONTENTS

Page

Question Presented ..... *i*

Parties ..... *i*

Table of Contents ..... *ii*

Table of Authorities ..... *iii*

Petitioner's Reply Brief 1

Reply Arguments 2

I. The Mississippi Regulation in *Transco* and the Kansas Regulation in *Northern Natural* Differ Significantly from the Oklahoma Statutory and Regulatory Scheme. 2

A. The Mississippi and Kansas Schemes 2

B. The Oklahoma Scheme 4

II. Like the Regulation Involved in *Northwest Central*, Rule 1-305 Falls Within the Carefully Protected Sphere of Reserved State Power. 8

TABLE OF AUTHORITIES

Page

CASES

Cities Service Gas Co. v. Peerless Oil & Gas Co., 340 U.S. 179 (1950) 7

Northern Natural Gas Co. v. State Corporation Commission of Kansas, 372 U.S. 84 (1963) . . 2, 3, 4, 7, 9

Northwest Central Pipeline Corp. v. State Corporation Commission of Kansas, 57 U.S.L.W. 4302 (March 7, 1989) 2, 5, 8, 9, 10

Transcontinental Gas Pipe Line Corp. v. State Oil & Gas Board of Mississippi, 474 U.S. 409 (1986) 2, 3, 4, 7, 9

STATUTES

Okla. Stat. tit. 52, § 239 . . . . . 4, 6, 7, 8

Okla. Stat. tit. 52, § 240 . . . . . 2, 4, 6, 7, 8

REGULATIONS

Corporation Commission Order No. 281285 . . . 4, 6, 7

Mississippi Statewide Rule 48 3

OCC OGR 1-305 . . . . . 2, 5, 6, 7, 8, 9

SUPREME COURT RULES

Supreme Court Rule 21.5 1

Page

BRIEFS

Answer Brief of Appellee Corporation Commission of Oklahoma in *Panhandle Eastern Pipe Line Co. v. Corporation Commission,* Appeal No. 64890 ..... 4, 7

Reply Brief of Commission Conservation Division, Cause No. 28770 8

No. 88-1482

IN THE

Supreme Court of the United States

OCTOBER TERM 1988

THE CORPORATION COMMISSION
OF THE STATE OF OKLAHOMA,

Petitioner,

v.

ANR PIPELINE COMPANY, ET AL.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

PETITIONER'S REPLY BRIEF

Petitioner Corporation Commission of the State of Oklahoma ("Corporation Commission") submits this Reply Brief under S. Ct. R. 21.5 to address arguments first raised in the Respondents' opposing briefs. This Reply Brief is necessary to properly characterize Oklahoma's statutory and regulatory scheme. In seeking to minimize the uniqueness and importance of this case, Respondents have brushed aside both the delicate balance employed by this Court's pre-emption jurisprudence and Oklahoma's longstanding interpretation of the statutory and

regulatory scheme involved in this case as being a method of allocating production.

Each opposition brief filed by Respondents attempts to characterize Oklahoma Corporation Commission Oil and Gas Rule 1-305 and Okla. Stat. tit. 52, § 240 as ratable purchasing provisions. Once attaching that semantic label to the regulatory scheme, Respondents argue that the provisions are pre-empted under *Northern Natural Gas Co. v. State Corporation Commission of Kansas,* 372 U.S. 84 (1963) and *Transcontinental Gas Pipe Line Corp. v. State Oil & Gas Board of Mississippi,* 474 U.S. 409 (1986).

To the contrary, Rule 1-305, and the statutes underlying the rule, are devices to regulate and allocate production to existing available market demand. Far from being a pre-empted purchasing regulation, the Oklahoma statutory and regulatory scheme allocates production to prevent waste, promote conservation, protect public safety, and preserve correlative rights in the exact manner allowed and approved by this Court in *Northwest Central Pipeline Corp. v. State Corporation Commission of Kansas,* 57 U.S.L.W. 4302 (March 7, 1989).

REPLY ARGUMENTS

I. The Mississippi Regulation in *Transco* and the Kansas Regulation in *Northern Natural* Differ Significantly from the Oklahoma Statutory and Regulatory Scheme.

A. The Mississippi and Kansas Schemes.

In *Transco,* various working interest owners in six

wells sold their gas to Transco. Transco purchased not only from the owners with whom it had contracts but also from noncontracted owners. However, in the Spring of 1982, demand for gas decreased significantly and Transco, as a result, stopped purchasing from noncontracted owners. Shortly thereafter, one noncontracted owner petitioned the Mississippi Oil and Gas Board to enforce Statewide Rule 48, a ratable take rule whose sole purpose was to prevent drainage:

> Each person now or hereafter engaged in the business of purchasing oil or gas from owners, operators, or producers shall purchase without discrimination in favor of one owner, operator, or producer against another in the same source of supply.

The Gas Board found Transco in violation and ordered it to take gas ratably. *The effect of the Gas Board's order was to require Transco to purchase more gas than it had demand for.* To maintain its current purchasing patterns, Transco had to purchase additional amounts under the Gas Board's order. The effect was to increase Transco's take-or-pay obligations, with the cost ultimately borne by the consumer.

This Court held the Mississippi regulation to be unconstitutional because it was aimed directly at interstate purchasers and because it resulted in an increased price which would ultimately be borne by consumers. *Transco,* 474 U.S. at 421-22.

This Court's earlier decision in *Northern Natural* is very similar to *Transco.* In *Northern Natural,* Kansas at-

tempted to impose ratable purchasing on interstate pipelines in such a manner that they would be required to either take more gas from Kansas than the pipelines could currently use, or risk breaching their contracts by decreasing takes. *Northern Natural,* 372 U.S. at 89. As it did in the later *Transco* decision, this Court struck down the Kansas regulation because the means chosen "threatened effectuation of the federal regulatory scheme." *Northern Natural,* 372 U.S. at 93.

B. The Oklahoma Scheme.

The Oklahoma scheme differs markedly from Mississippi's. The purpose of Oklahoma's ratable take statute, Okla. Stat. tit. 52, § 240, is to ensure ratable production as required by Okla. Stat. tit. 52, § 239. The Corporation Commission's exercise of jurisdiction over interstate pipelines is therefore incidental to its jurisdictional mandate to regulate production pursuant to section 239 and is a tool for enforcing such production regulation. *See* Commission Order No. 281285, App. F at 66. *Unlike the Mississippi and Kansas schemes, Oklahoma does not require a purchaser to take more gas than its market demand.* Oklahoma's statutory scheme has *always* been defended by the Corporation Commission as a scheme to allocate *production. See* Answer Brief of Appellee Corporation Commission of Oklahoma in *Panhandle Eastern Pipe Line Co. v. Corporation Commission,* Appeal No. 64890, at 5. The purpose of Oklahoma's statutory scheme is to regulate production under sections 239 and 240. Through the authority of these statutes, the Commission

has established a production scheme designed exclusively to promote the legitimate state interests in preventing waste, promoting public safety, and protecting correlative rights. Purchasers have been impacted only incidentally, and for the sole purpose of assuring that the gas which is purchased is produced according to Oklahoma's priority and ratability allocation scheme—a scheme designed to meet Oklahoma's production objectives. Oklahoma's scheme therefore falls squarely within this Court's most recent analysis of permissible impact on matters subject to FERC control:

> Where state law impacts on matters within FERC's control, the State's purpose must be to regulate production or other subjects of state jurisdiction, and the means chosen must at least plausibly be related to matters of legitimate state concern.

Northwest Central, 57 U.S.L.W. at 4309.

Unlike Mississippi's regulation whose sole purpose was to prevent drainage, there are numerous reasons for Oklahoma's statutory scheme, only one of which is the prevention of drainage. Rule 1-305 was promulgated against this statutory scheme—a scheme characterized not as a purchaser control, but as a production allocation. Production must be allocated, not only to prevent drainage, and, in the case of distressed wells, the public safety, but more importantly to prevent waste of the State's valuable resources. Waste can take many forms:

1. Reduced production capabilities following the shutting in and reopening of a well.

2. Complete loss of production capabilities following the shutting in and reopening of a well.

3. Failure to produce and market one type of hydrocarbon for which demand exceeds supply (oil) because gas is associated with its production, a hydrocarbon for which supply exceeds demand.

The interrelationship between production and the pipeline was recognized in Rule 1-305, and emphasized in Order No. 281285.

> It must be emphasized that Section 240 does not stand alone in its application; that it must be read in conjunction with Section 239 as a means for accomplishing the state's objective.

Order No. 281285, App. F at 55.

> [It] seems only logical that when production is dictated by pipeline capacity and demand and limited by this agency's setting of an allowable, the pipeline must be an integral part of that production function and regulation. Section 239 sets forth the circumstances under which prorating occurs and Section 240 provides a means of enforcing proration requirements. In this regard, the exercise of jurisdiction over interstate pipelines is incidental to this Commission's statutory responsibilities to protect correlative rights and prevent waste, a function of the regulation of production. As such, any incidental effect on interstate pipelines and interstate commerce is permissible.

Order No. 281285, App. F. at 59-60.

This interrelationship, and Oklahoma's focus on allocating production, is what sets this case apart from *Northern Natural* and *Transco*. As the Corporation Commission noted in the *Panhandle* appeal:

> Important reasons exist for Oklahoma's regulatory scheme other than the prevention of drainage, Mississippi's sole purpose. The Transco Court, in reaffirming *Northern Natural Gas Co. v. State Corporation Commission,* 372 U.S. 84, 9 L.Ed.2d 601 (1963), once again recognized that "a state may adopt reasonable regulations to prevent economic and physical waste of natural gas' *Cities Service Gas Co. v. Peerless Oil & Gas Co.,* 340 U.S. at 185, 95 L.Ed. 190, 71 S.Ct. 215." *Id.* at 742. Such acceptable measures "target producers and production while ratable take requirements are 'aimed directly at interstate purchasers and wholesales for resale.' " *Id.* Under *Transco* and *Northern Natural,* Oklahoma's regulatory scheme is constitutional.

Answer Brief of Appellee Corporation Commission at 9-10.

Oklahoma allocates production by section 239, section 240, and Rule 1-305. That longstanding and often reaffirmed intent and interpretation readily distinguishes this case as involving a permissible production regulation that targets producers and production.

This position was further illustrated by the Oil and Gas Conservation Division in its defense of Rule 1-305 in the proceeding leading to Order No. 281285:

> Secondly, and most importantly, these ratable take provisions are essentially directed at producers of natural gas. It stands to reason that if takers are required to take ratably, then the producers are only permitted to produce ratably. It is the taker that controls the [valve] . . . that controls the production. If the taker can only take so much in light of its demand, then the producer can only produce that amount. . . . It is the Oil and Gas Conservation Division's position that the ratable take and priority regulations are targeted at producers and production of natural gas, and . . . will not impermissibly interfere with interstate commerce.

Reply Brief of the Commission Conservation Division (Cause No. 28770) at 3-4 (emphasis added). The Corporation Commission has never deviated from the position that sections 239 and 240 work in tandem to allocate production, and that Rule 1-305 is designed for that same allocation purpose.

II. Like the Regulation Involved in *Northwest Central*, Rule 1-305 Falls Within the Carefully Protected Sphere of Reserved State Power.

Respondents argue that *Northwest Central* stands for the proposition that any regulation with an effect directed at a purchaser is pre-empted. This semantic argument overlooks the more thoughtful approach espoused by this Court in *Northwest Central.* In *Northwest Central,* this Court approved a regulation that had the purpose of instilling incentives in interstate purchasers to take gas and

had the effect of causing interstate purchasers to take gas. *Northwest Central,* 57 U.S.L.W. at 4305. In essence, Kansas acted to prevent the interstate pipelines from using Kansas gas fields to store low cost gas. *Id.*

This Court illustrated in *Northwest Central* its willingness to look at the substance of a regulation, and to analyze it, without use of the meaningless, semantical nuances advanced by Respondents in their opposition briefs. In *Northwest Central,* this Court emphasized that the field states are pre-empted from entering encompasses direct regulation of pipelines in such a way to affect their cost structures. *Northwest Central,* 57 U.S.L.W. at 4307. *See also Transco,* 474 U.S. at 422-23; *Northern Natural,* 372 U.S. at 94. However, finding pre-emption simply because costs and rates might be affected would nullify States' control over production. *Northwest Central,* 57 U.S.L.W. at 4308. Instead, this Court emphasized that it must be determined whether the regulation in question was a production regulation. The regulation is not pre-empted if it falls within the "traditional powers [of the States] to regulate rates of production, conserve resources, and protect correlative rights." *Northwest Central,* 57 U.S.L.W. at 4308.

Oklahoma's statutory scheme is a production scheme. Rule 1-305 is a regulation that allocates production to limited market demand. The regulatory scheme clearly falls within the permissible area of regulation left to the States in both the NGA and the NGPA, unrestricted by *Northern Natural* and *Transco,* and strongly reaffirmed by *Northwest Central.* This Court should grant certiorari to

confirm the scope of the powers retained by the States, or alternatively grant certiorari to remand this case to the Tenth Circuit for reconsideration in light of the *Northwest Central* decision.

Respectfully submitted,

Lindil C. Fowler, Jr., Esq.
General Counsel
Oklahoma Corporation Commission
400 Jim Thorpe Building
2101 North Lincoln Boulevard
Oklahoma City, Oklahoma 73105
(405) 521-2255

Counsel for Petitioner